

Danske Daily

US yield curve inverts

Market movers today

- Markets will continue to follow the tense situation in Hong Kong, where there are signs that China is mobilising forces close to Hong Kong. Should China move in, market sentiment would take a considerable hit, sending stocks, emerging market assets and yields lower.
- In the US, we expect a decent retail sales (control group) increase of 0.4% m/m, which is lower than in recent months, however. Consumption fundamentals still seem solid, with increasing employment, solid real wage growth and high consumer confidence. Private consumption is still the main growth driver in the US. That being said, the retail sales indicator is very volatile and prints negative from time to time despite consumption actually growing when looking at the bigger picture, so in that sense we would not be surprised if we get one bad print after some strong months. The numbers for manufacturing production will also be in focus given the difficulties for the sector amid the ongoing trade war with China. For the same reasons, we keep an eye on the release of the Empire PMI manufacturing.
- The main event in the Scandi region today is the Norges Bank monetary policy meeting despite it being a so-called ‘interim’ meeting (see page 2 for more details).

Selected market news

The global fixed income rally has continued unabated over the last 24 hours as risk appetite remains severely under pressure as markets react to rising tensions around Hong Kong, intensifying Brexit fears, second thoughts over whether the Trump China tariff exemptions are of any importance and, not least, as the macroeconomic backdrop in both Europe and China continues to weaken. Both the US and UK 2s10s government curves inverted for the first time since the financial crisis and 30Y treasury yields dropped below 2% for the first time ever in a staggering 18bp drop measured since Wednesday morning. The market is now pricing close to 100bp cumulative Fed cuts over the next 12 months. The yield curve inversion has put focus on the risk of a recession over the coming years and further weighed on risk sentiment, leading to a 3% drop in US equities, a 4% drop oil prices and a sharp rebound in the yen.

US President Donald Trump yesterday made comments about progress in the trade war on twitter, saying: “The American consumer is fine with or without the September date, but much good will come from the short deferral to December” and “Of course China wants to make a deal. Let them work humanely with Hong Kong first”.

In a video post yesterday, St Louis Fed’s Bullard made some general comments about the US economy and shared his thoughts on the Fed’s ongoing review of its monetary policy framework. He called current economic conditions good and suitable for a strategic review. He further said that a key focus should be to avoid getting stuck with an inflation rate below target and that negative interest rates could be looked at.

Selected reading from Danske Bank

- *Norges Bank Preview - Global turmoil calls for vaguer rhetoric*
- *Flash Comment Emerging markets: forget Argentina; focus on Fed, Trump and China*

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Scandi markets

In Norway, the monetary policy meeting is a so-called ‘interim’ meetings, with no press conference or monetary policy report and we do not expect any change to rates. As global risks have increased and domestic data has been a bit disappointing, we expect Norges Bank to reiterate its message from June that “the policy rate will most likely be increased further in the course of 2019”, without any explicit mention of September. This would keep the option of a September hike open while giving the bank scope to postpone if the current uncertainty persists or worsens.

Fixed income markets

The factors that pushed yields lower and flattened global curves (see front page) remain intact and we see more of the same in the next couple of weeks. Note also that despite equity futures being slightly in green overnight, yields have not corrected higher this morning. We expect a positive opening for EGBs this morning.

Despite the poor risk appetite, periphery managed to outperform core as the struggle to avoid negative yields clearly dominated. BTPs outperformed after the sell-off last Friday, as the ‘vote of no-confidence’ was delayed until Tuesday next week. The next focal point in Italy will now be Prime Minister Conte in Parliament on Tuesday, where he can either call the no-confidence vote or hand in his resignation to the President. We continue to prefer the sub 2y segment in Italy with the 2y bond yield still in positive territory.

FX markets

The relief in Scandi FX after the US tariff delay proved shortlived. EUR/SEK did dip further slightly on the stronger Swedish CPI print yesterday, but the move was only a knee-jerk and the trend higher in EUR/SEK swiftly resumed on the back of yesterday’s risk sell-off. Today, focus is on Norges Bank (even if this is a ‘small’ interim meeting only): the NOK may see some temporary support if Norges Bank comes out on the hawkish side signalling another rate hike in H2. However, price action in SEK around the Swedish CPI release yesterday may provide a blueprint for how the market will trade EUR/NOK on such an outcome: if markets are still in risk-off mode around today’s announcement, this is likely to overshadow any hawkish tilt.

Meanwhile, EUR/DKK dropped below the 7.46038 central rate yesterday for the first time since March. The drop might be due to early positioning ahead of the September ECB meeting, where most local banks are now calling for Danmarks Nationalbank (DN) to ease less than the ECB; this would create potential for EUR/DKK to sell off (see our take on page 14 of last week’s *Reading the Markets Denmark*). As we highlighted on Monday, Novo Nordisk is paying its semi-annual dividends in August (ex date tomorrow and date payable on Tuesday), which normally pushes EUR/DKK higher – historically around 20pips.

Finally, in the majors, USD/JPY and EUR/CHF both retreated yesterday as markets faded the relief rally after Tuesday’s US tariff delay and as the inversion of the 2Y10Y US and UK yield curves flashed recession signals and weighed on equities. We maintain a negative USD/JPY bias short term: we do not see the tariff delay as a game changer for souring risk sentiment and short USD/JPY is not (yet) a crowded trade according to recent positioning data, and, notably, the correlation of the cross with risk sentiment looks cleaner in USD/JPY compared to e.g. EUR/USD. Today’s US retail sales could prove interesting for near-term direction: in the past couple of months, this has moved USD/JPY around +/- 10-15pips, but the potential move may be higher today as volatility has picked up.

Key figures and events

Thursday, August 15, 2019				Period	Danske Bank	Consensus	Previous
3:30	AUD	Employment change	1000	Jul		14	0.5
6:30	JPY	Industrial production, final	m/m y/y	Jun			-3.6% -4.1%
8:00	SEK	Prospera inflation expectations					
8:00	NOK	Trade balance	NOK bn	Jul			5.2
10:00	NOK	Norges Banks monetary policy meeting	%		1.25%	1.25%	1.25%
10:30	GBP	Retail sales ex fuels	m/m y/y	Jul		-0.3% 2.3%	0.9% 3.6%
14:30	USD	Unit labour cost, preliminary	q/q	2nd quarter		1.8%	-1.6%
14:30	USD	Philly Fed index	Index	Aug		10.0	21.8
14:30	USD	Retail sales control group	m/m	Jul		0.4%	0.7%
14:30	USD	Initial jobless claims	1000				209
14:30	USD	Empire Manufacturing PMI	Index	Aug		2.0	4.3
15:15	USD	Capacity utilization	%	Jul		77.9%	77.9%
15:15	USD	Industrial production	m/m	Jul		0.3%	0.0%
15:15	USD	Manufacturing production	m/m	Jul		-0.3%	0.4%
16:00	USD	NAHB Housing Market Index	Index	Aug		66.0	65.0
22:00	USD	TICS international capital flow, Net inflow	USD bn	Jun			32.9

Source: Bloomberg, Danske Bank

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